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FISCAL IMPACT STATEMENT

LS 6298

BILL NUMBER: HB 1090

NOTE PREPARED: Feb 02, 2004

BILL AMENDED: Jan 29, 2004

SUBJECT: Rental Property Valuation and Tax Deductions.

FIRST AUTHOR: Rep. Buell

FIRST SPONSOR:

BILL STATUS: CR Adopted - 1st House

FUNDS AFFECTED: X GENERAL
X DEDICATED
FEDERAL

IMPACT: State & Local

STATE IMPACT	FY 2004	FY 2005	FY 2006
State Revenues		(44,000)	(88,000)
State Expenditures		(2,766,650)	(9,360,000)
Net Increase (Decrease)		2,722,650	9,272,000

Summary of Legislation: (Amended) *Assessment of Low-Income Rental Housing*: This bill establishes standards for the determination of the true tax value of low income rental housing.

Rental Unit Deduction: The bill provides that the property tax deduction for a building that contains principal rental dwellings is equal to the number of units multiplied by \$2,000.

Standard Homestead Deduction: The bill increases the standard deduction for homesteads by \$2,000.

Farmland Credit: The bill also establishes a farmland property tax credit. The bill makes an appropriation to distribute an amount to taxing units equal to the amount of farmland property tax credits granted in the taxing units.

PTRC and Homestead Credit Limit: This bill provides that the payment of Property Tax Replacement Credits (PTRC) plus Homestead Credits may not exceed \$2,000 for a homeowner in a year.

Effective Date: March 1, 2004 (retroactive).

Explanation of State Expenditures: *PTRC and Homestead Credit:* The overall impact to the state Property Tax Replacement Fund (PTRF) from all provisions of the bill is estimated to be a reduction in state expenditures of about \$2.8 M in FY 2005, and \$9.4 M in FY 2006. The following table summarizes the changes.

Estimated Change in Property Tax Replacement Fund Expenditures		
Provision	FY 2005	FY 2006
Rental Unit Deduction	\$150,000	\$450,000
Standard Homestead Deduction	(1,500,000)	(4,450,000)
Farmland Credit	23,333,350	70,000,000
PTRC and Homestead Credit Limit	(24,750,000)	(75,350,000)
Total PTRF Expense Impact	(\$2,766,650)	(\$9,350,000)

***Rental Unit Deduction:* The change in expenditures from the Property Tax Replacement Fund caused by the rental deduction is estimated at an increase of \$150,000 in FY 2005 and \$450,000 per year thereafter.**

The new deductions for rental property in this proposal would cause an increase in homesteaders' property tax bills which would result in an additional cost to fund the homestead credit. The homestead credit expenditure increase is estimated at \$325,000 in FY 2005 and \$970,000 per year thereafter.

The increased deductions would also cause part of rental property tax burdens to be shifted to business personal property beginning in CY 2005. The state pays the 60% school general fund PTRC on all property, however, business personal property does not qualify for the regular 20% PTRC. The state's expense for PTRC would be reduced by an estimated \$175,000 in FY 2005 and \$520,000 in all other years.

***Standard Homestead Deduction:* The state would have reduced expenditures for PTRC and Homestead Credit expenditures under the standard homestead deduction provision, estimated at \$1.5 M in FY 2005 and \$4.5 M per year following.**

The increased deductions for homesteads in this proposal would cause a reduction in homesteaders' property tax bills which would result in a reduced cost to fund the homestead credit. The homestead credit expenditure reduction is estimated at \$1.2 M in FY 2005 and \$3.6 M per year thereafter.

The increased deductions would also cause part of homeowners' tax burdens to be shifted to business personal property beginning in CY 2005. Therefore, the state's expense for PTRC would be reduced by an estimated \$280,000 in FY 2005 and \$835,000 in all other years.

Farmland Credit: Under this provision, farms that are at least 10 acres in size and owned by an individual (or a family) and is actively farmed by the individual (or family) may be eligible for a credit against property taxes on the farm land. Beginning in CY 2005, the credit would equal \$70 M per year, statewide. The \$70 M would be distributed to eligible farms on a pro-rata basis using the average assessed value per acre with a maximum of 250 acres per owner. A farmland owner may receive the credit on only one farm in the state.

The credit would be paid from the Property Tax Replacement Fund. **The cost of the credit would be \$23.33 Min FY 2005 (partial year) and \$70 M per year thereafter.** The bill appropriates \$23.33 M in FY 2005.

PTRC and Homestead Credit Limit: Under this bill, beginning in CY 2005, homeowners would not be able to receive more than \$2,000 per year in combined PTRC and Homestead Credits. It is estimated that this limitation would reduce PTRF expenditures by about \$74 M in CY 2005. On a fiscal year basis, the reduction in PTRF expenditures from the limitation are estimated at \$24.8 M in FY 2005 (partial year), \$75 M in FY 2006, and \$80 M in FY 2007.

Explanation of State Revenues: The state levies a small tax rate for State Fair and State Forestry. Any reduction in the assessed value base will reduce the property tax revenue for these two funds. **The total state property tax revenue reduction under this bill is estimated at \$44,000 in FY 2005 (partial year) and \$88,000 in all other years.** These revenue losses are broken down as follows:

Rental Unit Deduction: The reduction in state revenue caused by the rental deduction is estimated at \$17,000 in FY 2005 (partial year) and \$34,000 per year beginning in FY 2006.

Standard Homestead Deduction: The reduction in state revenue caused by the rental deduction is estimated at \$27,000 in FY 2005 (partial year) and \$54,000 per year beginning in FY 2006.

Explanation of Local Expenditures:

Explanation of Local Revenues: *Assessment of Low-Income Rental Housing:* The bill would limit assessors to the use of the capitalization of income method on low-income rental housing and would prohibit consideration of tax credits or government subsidies in determining the value of this property.

Under SEA 1-2004, all rental property with more than four units must be valued under the approach (cost, sales, or income capitalization) that yields the lowest valuation. The income capitalization approach would most likely yield the lowest assessment for low-income rental housing and would probably be used even in the absence of this proposal.

The restrictions on the income considered could reduce the value of some low-income rental property in certain situations. There is a great deal of uncertainty surrounding the issue of when and how subsidies are to be considered under current statutory law, current case law, and the new market value assessment rule. Currently, the assessment of low-income housing property under the income method might or might not consider the income from subsidies. Under this bill, these assessments definitely would not consider subsidy income.

Rental Unit Deduction: Under this proposal, each building containing rental property would be eligible for a property tax deduction equal to \$2,000 for each rental unit in the building. According to Census, there are about 709,100 rental units in Indiana. At \$2,000 each, the total deduction is estimated at \$1,420 M AV.

The rental deduction would cause a net property tax shift from rental properties to all properties in the approximate amount of \$28.1 M in CY 2005 and \$27.3 M in CY 2006. Approximately 30% of this amount (\$8.4 M in CY 2005) would be shifted to homeowners.

Total local revenues, except for cumulative funds, would remain unchanged. The revenue for cumulative funds would be reduced by the product of the fund rate multiplied by the AV reduction amount applicable

to that fund.

Standard Homestead Deduction: Under this proposal, the standard homestead deduction would be increased from the current \$35,000 to \$37,000 beginning in CY 2005. The \$2,000 increase in the deduction would result in a reduction of assessed value estimated at \$2,270 M AV in CY 2005 and years following.

The additional standard homestead deduction would cause a property tax shift from homeowners to all properties in the approximate amount of \$45.0 M in CY 2005 and \$43.7 M in CY 2006. Approximately 30% of this amount would actually be shifted back to homeowners bringing the net shift from homeowners to other property types to about \$31.5 M in CY 2005 and \$30.6 M in years following.

Total local revenues, except for cumulative funds, would remain unchanged. The revenue for cumulative funds would be reduced by the product of the fund rate multiplied by the AV reduction amount applicable to that fund.

State Agencies Affected: Department of Local Government Finance.

Local Agencies Affected: County and township assessors; County auditors.

Information Sources: Kurt Barrow, Director of Assessments, Department of Local Government Finance, (317) 232-3777; Census of Farming and Dataset: SF3, Tables: H7 and H30, U.S. Census Bureau; Local Government Database.

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